INTERCO

APPAREL · GENERAL RETAIL · FOOTWEAR

A DECADE OF UNINTERRUPTED GROWTH

ANNUAL REPORT
Fiscal Year 1974

INTERCO...

Manufacturers and Retailers of Popular-Priced Consumer Products and Services

63rd Annual Report

APPAREL MANUFACTURING GROUP

Designs, manufactures and distributes a full range of popular-priced branded and private-label sportswear and casual apparel for men and women; western wear and shirts for the entire family; and matched sets for work and leisure wear. Sportswear and casual apparel is produced in 44 apparel manufacturing plants and shipped to our customers from 8 major distribution centers.

The principal products for men include: woven and knit slacks, knit shirts—both sport and dress, sport coats, coordinated duo and trio sportswear, sweaters, jeans, western wear, outerwear, swim trunks, and walk shorts. For women: sweaters, slacks, skirts, vests, jackets, shirts and jeans.

GENERAL RETAIL MERCHANDISING GROUP

Operates 626 retail stores in most regions of the country which offer to the entire family a wide assortment of popular-priced products and services for the growing middle-income population.

General retailing operations include both full-service and self-service junior department stores, discount stores, men's specialty apparel shops and supermarket-type hardware, lumber and building materials stores. Stores are supplied from 8 modern regional distribution centers.

FOOTWEAR MANUFACTURING AND RETAILING GROUP

Styles, manufactures and wholesales men's, women's and children's footwear in most major price categories in the United States and Canada, and manufactures and wholesales men's footwear in Australia. Facilities include 39 shoe manufacturing plants and 8 major distribution centers.

The company also operates 884 retail shoe stores and leased shoe departments in the United States, Canada, Mexico and soon in Australia.

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Ten Consecutive Years of Growth

- **IN SALES**
- **IN EARNINGS**
- **IN EARNINGS PER SHARE**

During the ten-year period 1964-1974, INTERCO implemented a planned program of growth which has produced increases in sales and earnings each year. These results have been achieved by constant internal expansion, plus profitable acquisitions.

Today, with sales in excess of one billion dollars and net earnings of over forty-seven million dollars, INTERCO looks forward to maintaining its position of leadership as a manufacturer and retailer of popular-priced apparel, footwear and other consumer products and services. At the end of this ten-year period:

- Net sales — $1.12 billion in 1974 — almost four times greater than $295 million in 1963.
- Net earnings — $47.0 million in 1974 — almost nine times greater than $5.5 million in 1963.
- Earnings per share, fully diluted — $4.11 in 1974 compared to $0.82 ten years ago.
- Percent of net profit to sales — now 4.2% compared with 1.9% in 1963.
- Working capital is $314 million — up $196 million or 166% since 1963.
- Total assets are $547 million — up $349 million or 176% in the ten-year period.
- Long-term debt is 15% of invested capital compared to 32% in 1963.
- Shareholders' equity is $359 million — up $248 million or 223% since 1963.
- Return on shareholders' investment was 13.6% in 1974 and 4.9% in 1963.

ANNUAL MEETING OF STOCKHOLDERS
will be held at 10 a.m. on June 17, 1974

Stouffer's Riverfront Inn
200 South 4th Street, St. Louis, Missouri

Notice of the meeting and proxy statement will be sent to stockholders in a separate mailing.

HIGHLIGHTS OF THE YEAR

FISCAL YEARS ENDED FEBRUARY 28,	1974	1973	CHANGE
From operations:			
Net sales	**$1,121,927**	$1,051,189	+ 6.7%
Earnings before income taxes	**90,057**	82,668	+ 8.9%
Net earnings	**47,042**	42,471	+10.8%
Percent of net sales	**4.2%**	4.0%	
Per share of common stock:			
Fully diluted earnings	**$4.11**	$3.70	+11.1%
Dividends	**$1.32**	$1.25	+ 5.6%
Financial condition at year end:			
Working capital	**$ 314,044**	$ 293,055	+ 7.2%
Current ratio	**3.8 to 1**	3.7 to 1	
Total assets	**546,900**	510,884	+ 7.0%
Stockholders' equity	**359,350**	327,228	+ 9.8%
Return on stockholders' average investment	**13.6%**	13.5%	
Shares outstanding at year end:			
Common stock	**10,919,780**	10,874,872	
Preferred stock	**169,693**	177,357	
Number of stockholders	**15,700**	16,000	
Number of employees	**43,500**	42,600	

(Dollars in thousands except per share data)

To Our Stockholders:

The past year was an unusual one for American business because of an inflationary economic environment, product and raw material shortages, constantly increasing cost of doing business, and wage and price controls. However, at INTERCO, we had another record performance, completing a decade of uninterrupted improvement in sales and earnings.

INTERCO's performance for fiscal February 28, 1974, was the result of each of our three operating groups . . . Apparel Manufacturing . . . General Retail Merchandising . . . and Footwear Manufacturing and Retailing . . . contributing record high sales and earnings, despite the many difficulties beyond our control.

The achievements of the company over the past decade are the result of professional management in our operating divisions, sound employment of our assets, aggressive cost control programs in all phases of our business, and a plan for continued growth. Our growth program includes internal expansion for existing products and services and continuous evaluation of new acquisitions which will provide additional marketing opportunities.

When our diversification program was initiated ten years ago, certain fundamental guidelines were established and we have adhered to these principles which have made possible a portion of the improvement in the return on the shareholders' investment in INTERCO. One of the significant successes of our acquisition program, in addition to continuously higher sales and new earnings' records each year, is that the managements which joined INTERCO through the years, remain intact.

To monitor the complexities of our growing company, the Office of the Chief Executive, as shown below, establishes corporate policy, provides for continued long-term growth, and

Office of the Chief Executive: *Left to right:* W. L. Edwards, Jr., Senior Executive Vice President and Chief Administrative Officer; M. R. Chambers, Chairman of the Board and Chief Executive Officer; J. K. Riedy, President and Chief Operating Officer.

directs the administration of the company. This group includes the Chairman of the Board and Chief Executive Officer, the President and Chief Operating Officer, and the Senior Executive Vice President and Chief Administrative Officer.

We have proven management teams in each of our operating divisions. Communication within INTERCO is given constant emphasis and will continue to be given prime attention. We have given divisional management maximum operational decision-making responsibility and full earnings accountability, which offer high incentive for personal satisfaction. Budgeting, forecasting and regular monthly meetings of the Operating Board at corporate headquarters, provide the forum for the frequent sharing of the newest manufacturing and retailing techniques, and the exchange of marketing and styling trends.

The principal business of INTERCO is the manufacturing and retailing of popular-priced products and services—which are everyday basic necessities for the middle-income range of our population—and does not necessarily depend on a booming economy to maintain its position and to grow.

During the past year, capital expenditures amounted to $24.0 million, the highest in our history. This was the result of growing consumer demand for sportswear and casual apparel, an increasing market for our footwear products and expansion of new retail stores in many new communities.

In fiscal year ending February 28, 1975, we are budgeting capital expenditures of $18.5 million. At this time, we plan to open more than 100 new retail locations, both general retail and footwear stores and leased departments.

In January, 1974, two acquisitions were completed—each providing new business opportunities—continuing our prime goal to profitably expand the base of operations. Devon Apparel, Inc., a manufacturer and distributor of a diversified line of coordinated sportswear for women, was acquired in an exchange of stock on January 11, 1974. INTERCO's chain of men's specialty retail apparel stores was again expanded on January 31, 1974, with the acquisition of United Shirt Distributors, Inc. of Detroit, Michigan, also in an exchange of stock. United provides INTERCO with an entry into a new geographical retail area.

For a full report on the affairs of your company, we call your attention to the financial review commencing on page five and to the review of operations which is covered in pages nine through twenty-one of this report.

The quarterly dividend rate on common stock was increased twice within a nine-month period in 1973—January 5 and October 5, 1973, and these increases were in accordance with the government's Committee on Interest and Dividends. The Board of Directors will continue to evaluate the rate of the common stock dividend from time to time.

INTERCO is confident about its long-range future. Our financial position is excellent; we have the necessary discipline for continuous cost control and productivity improvement; and we have the competitive quality products and services for our consumers.

As we look ahead to the new fiscal year, we see many demanding and challenging areas in managing the business. However, our prime objective continues to stress improved return on stockholders' investment. We expect to maintain our position of leadership in the industries where we compete.

Working together, INTERCO achieved the best year in its history. We are grateful to our customers and suppliers, our fine employees, and our stockholders for their continuing support.

Respectfully submitted,

M. R. Chambers

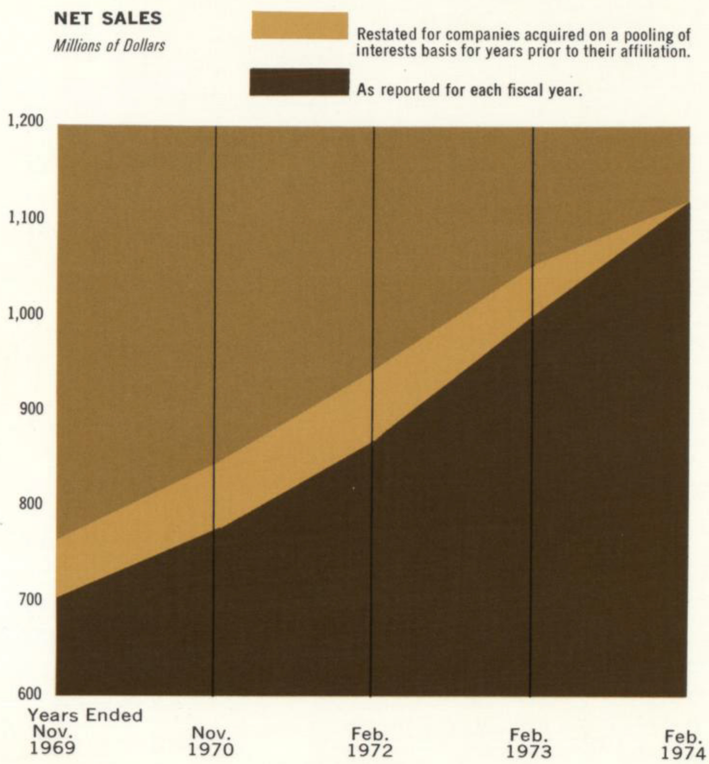
Chairman of the Board
and Chief Executive Officer

April 8, 1974

Fiscal 1974 in Review

FISCAL 1974 IN REVIEW

NET SALES
Millions of Dollars



INTERCO ended Fiscal 1974 in the strongest financial position in its history. Sales of $1.12 billion, net earnings of $47 million, and earnings per share of $4.11, fully diluted, established new records for the tenth successive year.

The comparative financial statements for fiscal 1973, reflected in this report, have been restated to include the acquisition of companies during fiscal 1974 by the issuance of common stock, and accounted for as poolings of interests.

SALES

Net sales for the year ended February 28, 1974, were $1.12 billion, an increase of 6.7% over the restated sales of $1.05 billion for fiscal 1973. Net sales reported for fiscal 1973 were $1.00 billion.

Each of INTERCO's three operating groups reported record high sales in fiscal 1974, as shown below in millions of dollars:

	Fiscal 1974		Fiscal 1973		%
	Sales	%	Sales	%	Increase
Apparel	$ 281.1	25.1	$ 266.0	25.3	5.7
General Retail	363.2	32.4	342.6	32.6	6.0
Footwear	477.6	42.5	442.6	42.1	7.9
Total	$1,121.9	100.0	$1,051.2	100.0	6.7

Sales of the company increased $70.7 million during fiscal 1974, and each of the three operating groups contributed approximately the same percentage increase.

EARNINGS

Earnings before income taxes for fiscal 1974 were a record $90.1 million or 8.9% higher than the restated 1973 pre-tax earnings of $82.7 million, an increase of $7.4 million. The pre-tax earnings reported in fiscal 1973 were $75.8 million.

The pre-tax earnings of each of INTERCO's business groups, before corporate expenses and interest cost, are compared in millions of dollars:

	Fiscal 1974		Fiscal 1973		%
	Amount	%	Amount	%	Increase
Apparel	$ 30.7	30.6	$ 28.6	31.6	7.3
General Retail	23.8	23.8	18.2	20.1	30.8
Footwear	45.7	45.6	43.6	48.3	4.8
	100.2	100.0	90.4	100.0	10.8
Corporate expenses and interest cost	10.1		7.7		
Earnings before income taxes	$ 90.1		$ 82.7		

The most significant increase in pre-tax earnings in fiscal 1974 was made by the general retail group. This performance was the result of profit improvement during the year by practically all divisions within this group, and the benefits received from action taken in fiscal 1973 to liquidate a division of Central Hardware.

Corporate expenses and interest cost increased during fiscal 1974, resulting from costs related to acquisi-

tions, and higher interest expenses.

Net earnings for fiscal 1974 were a record $47.0 million, an increase of 10.8% over the restated net earnings of $42.5 million for fiscal 1973. The reported net earnings for fiscal 1973 were $39.1 million. The margin of profit—net earnings to sales—increased to 4.2% this year, as compared to 4.0% in the previous year.

This improvement was the result of increased volume of business, strict budgetary controls, maximizing opportunities while minimizing risk, and in-depth management of the assets of the company.

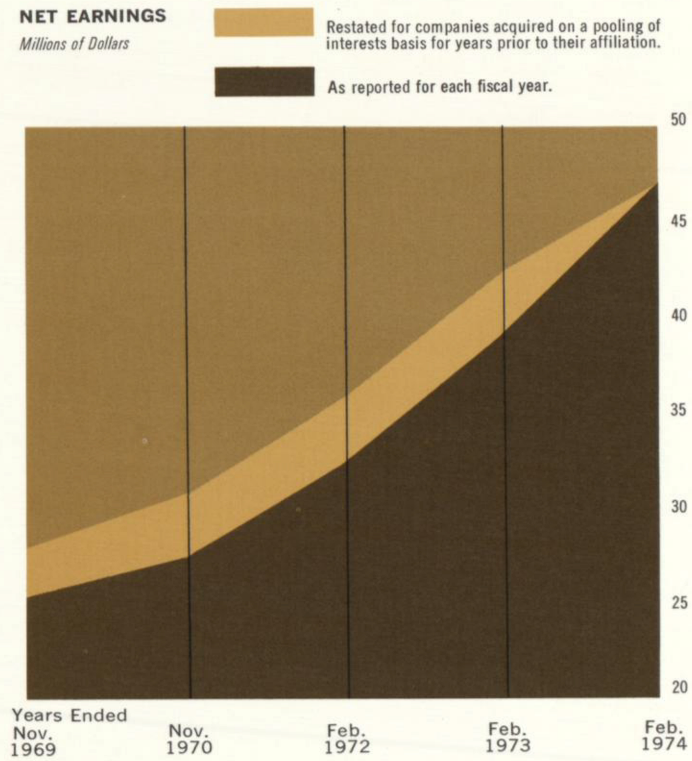
Fiscal 1974 net earnings were favorably influenced by a slightly lower effective income tax rate of 47.8%. This is primarily due to the tax benefit received from the "flow through" method of accounting for the investment tax credit, which amounted to $912,000.

Fully diluted earnings per common share were $4.11 for fiscal 1974, an increase of $0.41 per share or 11.1% over the restated per share of $3.70 in fiscal 1973. Fully diluted earnings per share reported for fiscal 1973 were $3.69.

FINANCIAL POSITION

The company's strong financial condition continued improvement in fiscal 1974, and at year-end:

- Working capital, the excess of current assets over current liabilities, reached a new high of $314.0 million, an increase of $21.0 million over the prior fiscal year.
- The ratio of current assets to current liabilities was 3.8 to 1 compared with 3.7 to 1 at February 28, 1973.
- Cash and marketable securities increased to $24.4 million, with no short-term borrowings.
- Accounts receivable increased to $149.3 million, higher by 4.0%. All of this increase is the result of increased sales volume in the fourth quarter of fiscal 1974.
- Inventories totaled $245.6 million compared with $232.4 million one year ago, an increase of 5.7%. The inventory increase is related to the new stores opened during the year and slightly higher inventories in the apparel manufacturing group.
- Long-term debt, less current maturities, at fiscal year-end 1974 was $63.1 million and represented 15% of the invested capital of the company.
- Stockholders' equity at February 28, 1974, was $359.4 million, an increase of $32.1 million over the restated stockholders' equity of one year ago.
- Return on average stockholders' equity was 13.6% for fiscal 1974.



FISCAL 1974 IN REVIEW

CAPITAL EXPENDITURES

Record high capital expenditures of $24.0 million were made during fiscal 1974. These expenditures met the growing demand for our products and services and included new shoe and apparel manufacturing plants and new retail stores, as well as expansion and modernization of existing manufacturing plants and the refurbishing of retail locations. The capital expenditures for the next fiscal year are budgeted at $18.5 million with depreciation of $12.5 million.

DIVIDENDS

During the fiscal year, dividends of $14.1 million were paid to shareholders, represented by $13.2 million to holders of common stock and the balance to preferred stockholders. On September 10, 1973, the Board of Directors increased the quarterly common stock dividend from $0.32 to $0.34 per share, increasing the annual common stock dividend rate to $1.36 per share. The 252nd consecutive quarterly common stock dividend of the company was paid on April 5, 1974, at the rate of $0.34 per share.

ACQUISITIONS

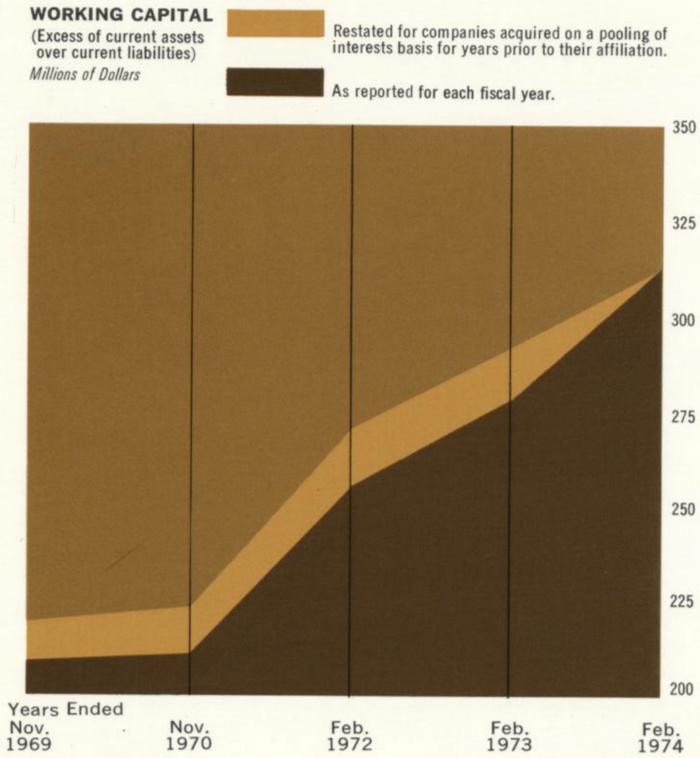
Two excellently managed companies were acquired by INTERCO during fiscal 1974.

- Devon Apparel, Inc. was acquired on January 11, 1974, in an exchange of 723,852 shares of INTERCO common stock for all of the outstanding capital stock of Devon.
- United Shirt Distributors, Inc. was acquired on January 31, 1974, in an exchange of 142,570 shares of INTERCO common stock for all of the outstanding capital stock of that company.

More detailed information on these companies can be found on pages nine through eleven.

ORGANIZATIONAL CHANGES

- Joseph Fox, who was a member of the Board of Directors and a Vice President of INTERCO, elected to retire early, on June 1, 1973.
- Charles J. Rothschild, Jr. became President of Campus Sweater & Sportswear Company on September 6, 1973, and was appointed to the Operating Board of INTERCO on September 10, 1973.
- Philip N. Hirsch, an INTERCO Director and Vice President, became Chairman of the Board of P. N. Hirsch & Company on February 1, 1974, and Gerald Hirsch became its President on the same date.
- Herbert Shainberg, Chairman of the Board of Sam Shainberg Company and a Vice President of INTERCO chose to retire from both of these positions on February 2, 1974. Mr. Shainberg will continue as a Director of the company.
- William Forman, President of Devon Apparel, Inc., became a member of the Operating Board of INTERCO on January 14, 1974.
- Barry S. Fine, President of Fine's Men's Shops, Inc. and Standard Sportswear, Inc., was appointed to the Operating Board of INTERCO on February 11, 1974.



Review of Operations

UNITED JOINS MEN'S APPAREL SHOPS

The growing chain of Men's Specialty Apparel Shops, which are part of the General Retail Merchandising Group of the company, was expanded during the year with the acquisition of United Shirt Distributors, Inc. on January 31, 1974.

United operates 39 men's apparel stores in the metropolitan Detroit, Michigan, area under the names of United and Jeans Galore. These stores, predominantly in shopping centers, carry an extensive line of popular-priced apparel and other male furnishings.

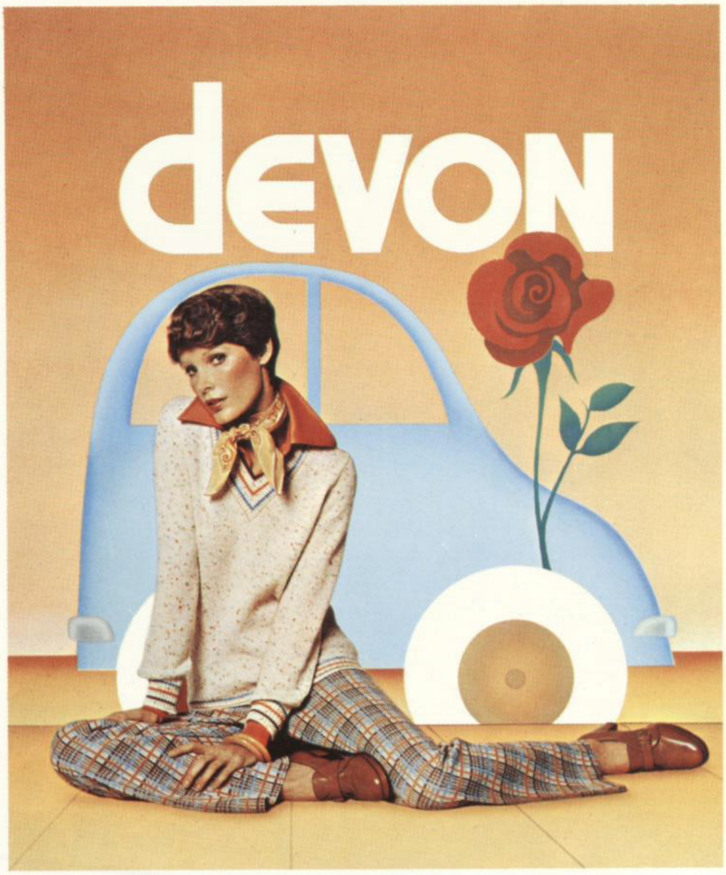
INTERCO now operates 67 men's specialty apparel stores in Michigan, North Carolina, Ohio, Pennsylvania, South Carolina, Virginia and West Virginia, under regional trade names of Fine's Men's Shops, Standard Sportswear, United and Jeans Galore.

Growth from this base of operations is unlimited and plans provide for the continual expansion of this chain of men's apparel shops throughout the geographical regions they now serve, as well as entering new regions.

Devon Joins Apparel Manufacturing Group

Devon Apparel, Inc. joined the Apparel Manufacturing Group of INTERCO on January 11, 1974. Devon, a major designer, manufacturer and distributor of a diversified line of contemporary coordinated sportswear for women, was founded in 1943 and has grown steadily over the years.

The addition of this division expands further the growing apparel operation of INTERCO, and adds new growth dimensions in a totally new area of its business—moderately-priced basic clothing for women—clothing with a strong fashion image. Devon's principal



products include sweaters, slacks, skirts, vests, jackets and shirts for the missy and the large-size sportswear market.

Devon's executive, marketing and styling offices are in Philadelphia, as well as its manufacturing and fully-automated customer service center. Its multiline branded products . . . DEVON and LADY DEVON . . . are sold nationally through more than 7,000 department and specialty stores.

Devon maintains showrooms and a designing office in New York City and regional sales offices in ten cities across the country. In addition, Devon is a totally integrated producer, which manufactures a large percentage of its material requirements.

Devon is programmed, with its extensive product lines, to the expanding demand for leisure apparel and is in an excellent position to capture and expand its share of the female sportswear market.

Shown on these pages are a few of the coordinated offerings of Devon.


CLOSTER

APPAREL MANUFACTURING GROUP

Fiscal 1974 was a significant year for the apparel business of INTERCO. Existing operations had record sales and earnings for the year, and a new dimension and opportunity for the future was added—women's sportswear manufacturing—through the acquisition of Devon Apparel, Inc.

The apparel group contributed $281.1 million or 25% of the sales, and $30.7 million or 30% of the earnings of the company, a return of 10.9% on sales before income taxes, corporate expenses and interest cost.

Shown on these pages are but a few of the wide range of apparel selections offered to the consumer for work and leisure time. Our principal products include a variety of moderately-priced fashions: woven and knit slacks, knit shirts—both sport and dress, sport coats, jackets, coordinated duo and trio sportswear, suits, sweaters, jeans, western wear, outerwear, swim trunks and walk shorts. The contemporary sportswear for women from Devon feature a coordinated line of sweaters, slacks, skirts, vests, jackets and shirts.

The apparel manufacturing industry continues to be fashion-oriented. Even though many of our products are considered "classics," we have the people who are necessary to provide creative merchandising and styling. This will enable the company to continue its outstanding growth and to be a major competitor in the market it serves.

A substantial part of the company's record capital expenditures during the year was used to expand and modernize the manufacturing and customer distribution capabilities of the apparel group. During fiscal 1974, eight new factories were added which increased our productive capacity by 20%. To meet the increasing customer interest in INTERCO's apparel prod-

APPAREL PLANTS

Beginning of Year	Added	Closed	End of Year
37	8	1	44

MAJOR APPAREL BRANDS: For men and young men: Big Yank • Biltwell • Campus • Cowden • Impact 70's • John Alexander • Leonard Macy • Mr. Golf • Mr. Tennis • Tailor's Bench. For women: Devon • Lady Devon. For the family: Big Yank.

ucts, present plans include several additional manufacturing plants during the new fiscal year which will increase our capacity another 10%.

Great emphasis is devoted to the development of new manufacturing techniques and technological improvements. Company-developed machines and devices are supplemented by the newest and most sophisticated knitting and sewing equipment from various parts of the world. Manufacturing efficiency has been improved by the introduction of automated equipment to several basic operations. New methods and machines are continually reviewed and tested to determine their practicability for greater productivity and improved quality.

The INTERCO apparel group combines all the necessary strengths to grow in the future and offers complete flexibility to act and react to the demands of the discriminating style-conscious and cost-conscious American consumer. Style, quality and value continue as INTERCO's guiding goal.

Leisure Time Wear

Jeans for the Family

GENERAL RETAIL MERCHANDISING GROUP

The general retail merchandising group contributed record high sales and earnings to the total INTERCO performance in fiscal 1974. This group reported $363.2 million or 32% of the sales of the company, and $23.8 million or 24% of the earnings—a return of 6.6% on sales before income taxes, corporate expenses and interest cost.

These retail stores offer a wide range of popular-priced consumer products and services for the expanding middle-income range of our population through 626 retail locations in most regions of the country. The general retail operations are represented by the following types of stores:

Junior Department Stores		
Full-service	**91**	
Self-service	**287**	**378**
Discount Stores		**157**
Men's Specialty Apparel Shops		**67**
Hardware, Lumber and Building Materials Supermarkets		**24**
Stores in Operation		**626**

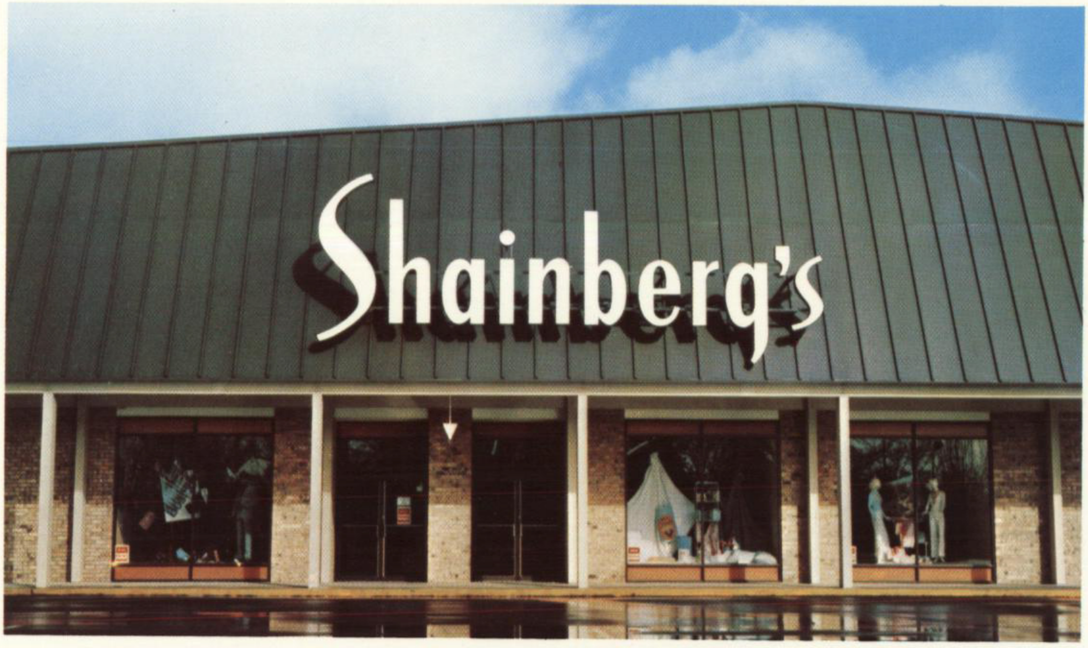
During fiscal 1974, the general retail merchandising group added 86 new locations, while closing marginal ones, and relocating others, and has plans to open a minimum of 50 new units during the 1975 fiscal year. To accommodate the growth of additional units each year, the company continues to emphasize and accelerate its planned employee program for in-depth internal training of store managers and other key people. This program maintains a pool of experienced personnel to facilitate profitable growth and expansion.

GENERAL RETAIL STORES

Beginning of Year	Added	Closed Relocated or Sold	End of Year
571	86	31	626

MAJOR RETAIL TRADING NAMES: Central Hardware • Carithers • Eagle Family Discount Stores • Fine's Men's Shops • Golde's • Hirsch Value Centers • Jeans Galore • Keith O'Brien • Kent's • Lin-Brook Hardware • Miller's • P. N. Hirsch • Shainberg's • Standard Sportswear • The I. D. Store • Thornton's • United • Wigwam.

GENERAL RETAIL MERCHANDISING GROUP



Aggressive merchandising policies, coupled with the ability to move merchandise swiftly from new, modern, fully-automated regional distribution centers to the retail units, provide our customers with competitive values in today's cost-conscious environment.

The junior department stores of INTERCO continue to expand into new communities in their regions, which are principally the Midwest, the Southeast, and the Northwest. The Hirsch chain, and Shainberg's, Golde's and Kent's stores concentrate on providing basic clothing and household needs to the consumer, and these will be expanded in the years ahead.

The Eagle Family Discount Stores, offering over 10,000 discount items for the family, were expanded again during the past year, and Eagle will continue to enter new communities in the southeastern part of the country.

Central Hardware, a leading supermarket-type hardware, lumber and building materials chain, posted the highest volume and earnings in its history. In addition, Central entered a new retail market—Memphis, Tennessee—late in the fiscal year with the opening of four large 70,000 square foot locations for the "Do-It-Yourselfer." This chain will be expanded, on an orderly basis, to meet the growing demand by value-conscious families for one-stop home improvement and home repair needs.

The general retail group of INTERCO enters fiscal 1975 confident of substantial future growth.

FOOTWEAR MANUFACTURING AND RETAILING GROUP

The footwear group of the company, which includes both manufacturing and retailing, reported record high sales and earnings in fiscal 1974. This group contributed $477.6 million or 43% of the sales, and $45.7 million or 46% of the earnings of the company—a return of 9.6% on sales before income taxes, corporate expenses and interest cost.

In this decade of uninterrupted growth for INTERCO, the footwear group—the original operations of the company—has grown in each of these years because it manufactures footwear of quality and fashion, and because of a continuation of internal expansion in the retail part of the business.

Footwear Manufacturing:

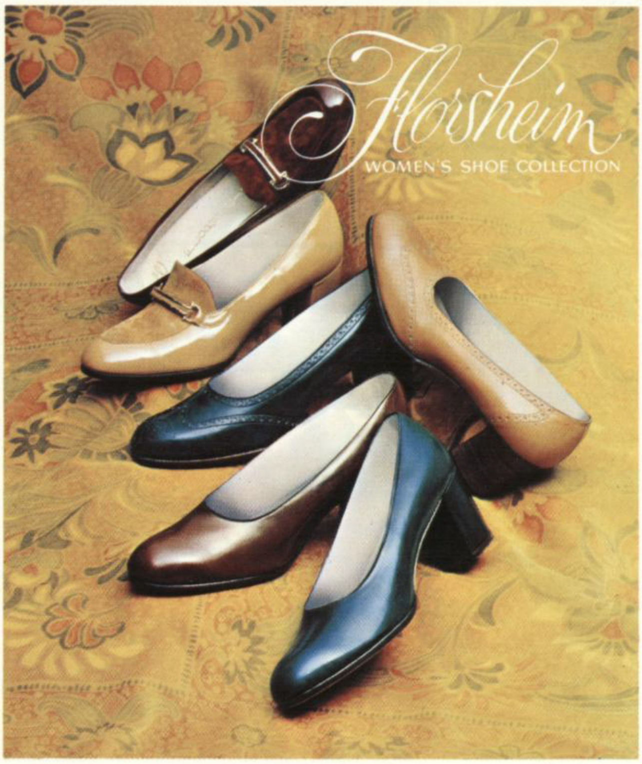
The divisions within this group style, manu-

	Beginning of Year	Added	Closed Relocated or Sold	End of Year
Manufacturing Plants	38	3	2	39
Shoe Stores and Leased Shoe Departments	873	71	60	884

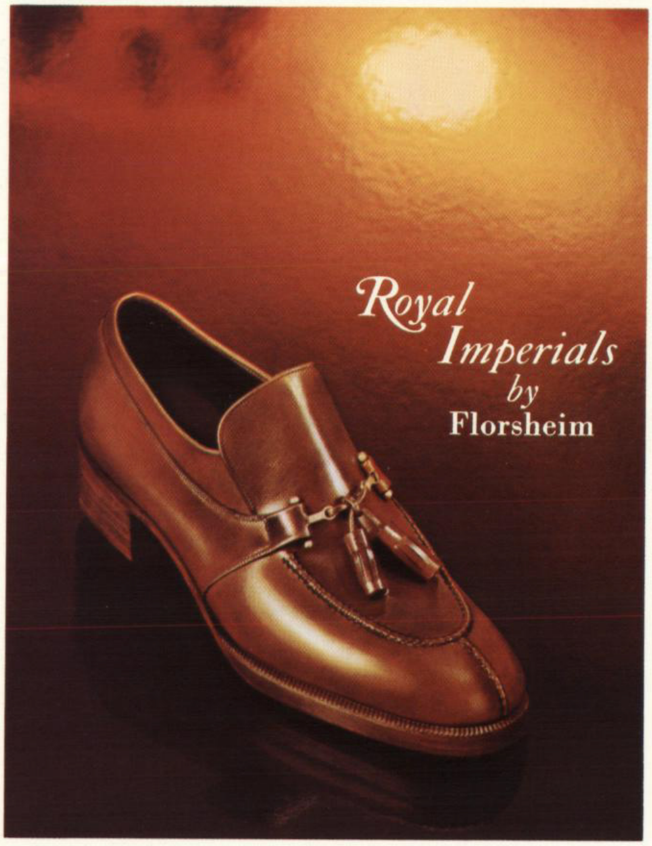
MAJOR FOOTWEAR BRANDS: For men: Ambassador • Florsheim—Florsheim Imperial and Royal Imperial • Hy-Test • Julius Marlow • McHale • Rand • Winthrop • Worthmore. For women: Denny Stewart • diVina • Florsheim • Imperial and Ramblers by Florsheim • Miss Wonderful • Personality • Thayer McNeil • Thomas Wallace • Vitality. For children: Red Goose • Poll Parrot • Savage.

MAJOR RETAIL TRADING NAMES: Florsheim Men's Shops • Duane's • Gude's • Paul's Shoes • Phillip's Shoes • Thayer McNeil Shoe Shops • Thompson, Boland & Lee.

facture, and wholesale men's, women's and children's footwear in most price categories in the United States and Canada, and manufacture and wholesale men's footwear in Australia, and include:



- The Florsheim Shoe—men's and women's—unchallenged leadership in the market it serves, emphasizing quality leather, quality fashion, and quality craftsmanship.
- International Shoe Company—increased its penetration into the popular-priced footwear market for men, women and children, providing both branded and private-label footwear.
- In Canada, Interco Savage manufactures men's and women's footwear, including Florsheim, and children's shoes for the Canadian market.



■ Julius Marlow Holdings, an Australian subsidiary, maintains a dominant position in Australian men's quality shoes, including the Florsheim shoe.

We continue to research and experiment for improved methods in the manufacturing of shoes. During the year, International Shoe and Florsheim Shoe installed a "gradamatic computer controlled footwear pattern grading and cutting system," which could revolutionize the grading of shoe patterns and provide improved efficiency and cost reductions.

Florsheim's strong business makes new production facilities necessary. During fiscal 1974, The Florsheim Shoe Company increased its production capacity by eight percent and, after the close of the fiscal year, purchased two additional manufacturing plants. These actions were necessary to meet the continued increasing demand for Florsheim's quality—all leather—shoes.

Footwear Retailing:

The footwear retailing operations of INTERCO continued to show growth in established units during the year, and added 71 new large attractive units, while continuing to close smaller marginal units and to relocate others. At year end, shoe stores and departments were in operation in most parts of the United States and Canada and in Mexico City.

Florsheim led the expansion program with the opening of 58 new Florsheim Men's Shops, Thayer McNeil Shoe Shops, and leased departments in all areas of the country. Three Florsheim Shoe Shops for men are now operating successfully in Mexico City, bringing the same high quality merchandise to the people of Mexico as found in those stores in the United States. Florsheim will open the first Florsheim Shoe Shop in Sydney, Australia, later this year.

The previously announced plan for the orderly transfer of certain regional retail footwear operations of International Retail Shoe—a former division of INTERCO—to Florsheim was completed during the year. Senack Shoe, the leased shoe department operation, remains intact and during the year continued to open new units, mostly in regional department stores.

Present plans provide for the opening of 50 new shoe stores and leased departments during fiscal 1975, which will bring the total shoe retailing operations of INTERCO to more than 920 units.

General:

The forward movement of INTERCO's footwear business in fiscal 1974 provided its most successful year, and this was a direct result of the sound organizing abilities of the managements which operate the footwear divisions. These results were possible, despite the margin-squeeze from economic regulation, escalating raw material costs, and extreme pressure on production facilities. Plans require continued expansion of our footwear group in the coming year.

INTERCO

Consolidated Financial Statements

consolidated balance sheet

(Dollars in thousands)

ASSETS

February 28,	1974	1973
Current assets:		
Cash	$ 13,045	$ 18,346
Marketable securities, at cost which approximates market	11,350	1,948
Receivables, less allowance for doubtful accounts and cash discounts of $4,210 ($3,682 in 1973)	149,277	143,477
Inventories:		
Finished products and other merchandise	180,887	175,333
Raw materials and work in process	64,741	57,042
	245,628	232,375
Prepaid expenses	3,163	2,830
Future income tax benefits	2,894	2,165
Total current assets	425,357	401,141
Excess of investment over equity in subsidiaries at acquisition, net of amortization	9,323	9,995
Sundry investments and other assets	6,049	5,553
Future income tax benefits	2,616	2,450
Property, plant and equipment, at cost:		
Land	5,078	5,083
Buildings and improvements	91,193	82,210
Machinery and equipment	101,996	92,014
	198,267	179,307
Less accumulated depreciation	94,712	87,562
Net property, plant and equipment	103,555	91,745
	$546,900	$510,884

See accompanying notes to consolidated financial statements.

LIABILITIES AND STOCKHOLDERS' EQUITY

February 28,	1974	1973
Current liabilities:		
Current maturities of long-term debt	$ 3,623	$ 3,627
Accounts payable and accrued expenses	94,825	89,760
Income taxes	12,865	14,699
Total current liabilities	111,313	108,086
Long-term debt, less current maturities	63,145	62,528
Deferred compensation and other deferred liabilities	10,156	10,202
Minority interests in subsidiaries	2,936	2,840
Stockholders' equity:		
Preferred stock, at stated and liquidating value:		
First preferred	453	929
Second preferred	15,836	15,836
	16,289	16,765
Common stock, at stated value	81,898	81,727
Capital surplus	41,825	41,591
Retained earnings	219,338	187,780
	359,350	327,863
Less common stock in treasury, at cost	—	635
Total stockholders' equity	359,350	327,228
	$546,900	$510,884

CONSOLIDATED STATEMENT OF EARNINGS

(Dollars in thousands except per share data)

Years Ended February 28,	1974	1973
Sales and other income:		
Net sales	$1,121,927	$1,051,189
Other income, net	10,152	8,036
	1,132,079	1,059,225
Deductions:		
Cost of sales	791,247	741,901
Selling, general and administrative expenses	244,915	229,548
Interest expense	5,479	4,729
Minority interests	381	379
	1,042,022	976,557
Earnings before income taxes	90,057	82,668
Income taxes	43,015	40,197
Net earnings	$ 47,042	$ 42,471
Per share of common stock:		
Fully diluted earnings	$4.11	$3.70
Primary earnings	$4.23	$3.83

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

(Dollars in thousands)

Years Ended February 28,	1974	1973
Working capital provided by:		
Net earnings	$ 47,042	$ 42,471
Depreciation	11,642	10,528
Future income tax benefits	(166)	228
Other, net	722	463
Operations	59,240	53,690
Disposal of property, plant and equipment	1,611	1,082
Issuance of common stock for conversion of preferred stock—contra below	476	4,291
Exercise of stock options	94	3,434
Working capital of purchased company	—	2,603
Issuance of long-term debt	4,425	900
	65,846	66,000
Working capital used for:		
Additions to property, plant and equipment	23,957	16,745
Increase in funds in escrow for construction	1,106	—
Cash dividends	14,487	13,217
Conversion of preferred stock—contra above	476	4,291
Reduction of long-term debt	3,808	7,101
Purchase of company	—	3,261
Purchase of company's stock	526	—
Other, net	497	504
	44,857	45,119
Increase in working capital	$ 20,989	$ 20,881
Working capital increased (decreased) by:		
Cash and marketable securities	$ 4,101	$ (23,748)
Receivables	5,800	22,404
Inventories	13,253	23,605
Other current assets	1,062	2,095
Notes payable	—	5,098
Current maturities of long-term debt	4	1,059
Accounts payable and accrued expenses	(5,065)	(7,332)
Income taxes	1,834	(2,300)
	$ 20,989	$ 20,881

See accompanying notes to consolidated financial statements.

CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

(Dollars in thousands) **Years Ended February 28, 1974 and 1973**

	Preferred Stock	Common Stock Issued	Common Stock In Treasury	Capital Surplus	Retained Earnings	Total
Balance February 29, 1972:						
As previously reported	$20,647	$71,268	$ (4,440)	$36,552	$150,122	$274,149
Adjustments for pooled companies		8,248	1,973	126	10,044	20,391
As restated	20,647	79,516	(2,467)	36,678	160,166	294,540
Net earnings					42,471	42,471
Cash dividends:						
Preferred stock					(988)	(988)
Common stock—$1.25 per share					(12,064)	(12,064)
By pooled companies prior to acquisition					(165)	(165)
Stock dividend:						
By pooled company prior to acquisition		50		45	(95)	
Conversion of preferred stock:						
Series A—31,238 shares	(3,123)	1,019		2,104		
Series B—29,028 shares	(1,161)	435		726		
Series C— 66 shares	(7)	2		5		
Issuance of 53,800 contingent common shares			1,545		(1,545)	
Exercise of stock options:						
Series C— 4,087 shares	409			(134)		275
Common—104,073 shares		705	287	2,167		3,159
Balance February 28, 1973, as restated	16,765	81,727	(635)	41,591	187,780	327,228
Net earnings					47,042	47,042
Cash dividends:						
Preferred stock					(868)	(868)
Common stock—$1.32 per share					(13,248)	(13,248)
By pooled companies prior to acquisition					(371)	(371)
Conversion of preferred stock:						
Series A—2,807 shares	(281)	91		189		(1)
Series B—4,857 shares	(195)	73		122		
Purchase of 13,204 common shares			(526)			(526)
Issuance of 30,317 contingent common shares			997		(997)	
Exercise of stock options:						
Common—5,958 shares		7	164	(77)		94
Balance February 28, 1974	$16,289	$81,898	—	$41,825	$219,338	$359,350

See accompanying notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

February 28, 1974 and 1973

1. **Significant Accounting Policies**—The company and its subsidiaries employ generally accepted accounting principles on a consistent basis to present fairly their consolidated financial position, results of operations, and changes in financial position. The major accounting policies of the company are set forth below.

Principles of Consolidation—The consolidated financial statements include the accounts of the company and all domestic and foreign subsidiaries. Foreign subsidiaries (principally Canadian) are not material in relation to consolidated financial position or results of operations. All material intercompany transactions have been eliminated in consolidation.

Inventories—The majority of the inventories are priced at the lower of cost (first-in, first-out) or replacement market. Certain of the inventories are priced on the "last-in, first-out" method. Had the "first-in, first-out" method been applied to all inventories, they would have been stated at approximately $268,898,000 and $254,157,000 at February 28, 1974 and 1973, respectively.

Depreciation—For financial reporting purposes, the company employs both accelerated and straight-line methods in computing depreciation. Approximately 73% and 75% of depreciation expense was computed on the straight-line method in 1974 and 1973, respectively.

Excess of Investment Over Equity in Subsidiaries—Cost in excess of net assets of companies acquired is being amortized on a straight-line basis, generally over 40 years.

Start-Up Expenses—Start-up expenses of new facilities are charged to operations in the year incurred.

Income Taxes—Deferred compensation, depreciation, profit on installment sales and certain valuation reserves and accruals are recognized for income tax purposes in years other than the years in which they are reported in the financial statements. Provision has been made for resulting deferred taxes and future tax benefits. Investment tax credits are reflected as a reduction of Federal income taxes for the period in which qualified property is placed in service.

It is the company's intent that the undistributed earnings of subsidiaries will either be reinvested in the subsidiaries or distributed tax-free to the parent company. Accordingly, no provision has been made for income taxes on such undistributed earnings.

2. **Business Combinations**—During 1974, the company acquired all the outstanding stock of Devon Apparel, Inc. and United Shirt Distributors, Inc. in exchange for 866,422 shares of company stock. These transactions were accounted for as poolings of interests, and accordingly the accounts of these companies have been included in the accompanying financial statements for 1974 and 1973. Consolidated net sales and net earnings for 1973, prior to restatement for these business combinations, were $1,001,817,000 and $39,122,000, respectively. The net sales and net earnings of these companies for 1974, prior to combining, were $51,565,000 and $3,236,000, respectively.

During 1973, the company acquired all the outstanding stock of Big Yank Corporation and Standard Sportswear, Inc. in exchange for 309,321 shares of common stock. These transactions were accounted for as poolings of interests, and accordingly the accounts of these companies have been included in the accompanying financial statements for 1973. The results of operations of these companies for 1973, prior to combining, are not material to consolidated results of operations. Also during 1973, a company was acquired for $3,261,000 cash in a transaction which was accounted for as a purchase.

3. **Long-Term Debt**—Long-term debt consists of the following:

	1974	1973
	(in thousands)	
4⅝% promissory installment notes, payable $1,875,000 annually, 1974-1989, and balance in 1990	$42,500	$44,375
6% promissory installment notes, payable $750,000 annually, 1974-1975, $1,250,000 annually, 1976-1979, and balance in 1980	8,625	9,375
4¾% obligation under long-term lease, payable in annual installments increasing from $260,000 in 1974 to $565,000 in 1991	7,165	7,415
Other debt at 2½% to 9¾% interest rates, payable in varying amounts through 1993	8,478	4,990
	66,768	66,155
Less current maturities	3,623	3,627
	$63,145	$62,528

Current maturities of long-term debt in the five years following February 28, 1974, are as follows (in thousands):

1975	$3,623
1976	3,555
1977	4,434
1978	3,897
1979	3,977

The 4⅝% note agreement restricts retained earnings of $43,810,000 as to payment of cash dividends on capital stock and the purchase, redemption or retirement of capital stock. The agreement also provides that no such payments be made unless consolidated working capital shall be at least $80,000,000.

4. **Preferred Stock**—The company's preferred stock is issuable in series. Authorized preferred stock consists of 577,060 shares of first preferred and 1,000,000 shares of second preferred without par value. Such stock is summarized as follows:

First Preferred Series B—$2.10 cumulative, with stated and involuntary liquidating value of $40 per share; issued 11,334 shares at February 28, 1974 and 16,191 shares at February 28, 1973, callable beginning in 1975 at $42.10, decreasing to $40.00 in 1985; convertible into 2 shares of common stock.

Second Preferred Series C—$5.25 cumulative with stated and involuntary liquidating value of $100 per share; issued 158,359 shares at February 28, 1974 and 1973; callable beginning in 1975 at $105.25, decreasing to $100.00 in 1985; convertible into 3.0534 shares of common stock.

At February 28, 1973, 2,807 shares of first preferred Series A were outstanding. These shares were converted into 12,190 shares of common stock in 1974.

5. **Common Stock**—The company's common stock consists of 30,000,000 shares authorized with stated value of $7.50 per share, of which 10,919,780 shares were issued at February 28, 1974, and 10,896,985 shares at February 28, 1973, including 22,113 shares in the treasury.

Shares of common stock were reserved for the following purposes at February 28, 1974:

	Number of Shares
Conversion of preferred stock	506,201
Common stock options:	
Granted	236,162
Available for grant	119,325
Contingent shares based on profit performance of acquired companies	60,125
	921,813

Under the company's stock option plans, certain key employees may be granted options (qualified, non-qualified, or a combination of both) to purchase shares of common stock. Qualified options granted under the plans may not be less than 100% of the fair market value of the common stock on the date an option is granted, and non-qualified options at not less than 85%. All options which have been granted are qualified, become exercisable in installments, and expire five years from date of grant.

Changes in options granted are summarized as follows:

	1974		1973	
	Shares	Average Price	Shares	Average Price
Beginning of year	172,831	$39.94	209,290	$34.11
Assumed options of pooled company	—	—	11,467	19.90
Options granted	88,189	37.78	57,247	47.85
Options exercised	(5,958)	16.01	(104,073)	30.28
Options cancelled	(18,900)	44.61	(1,100)	47.73
End of year	236,162	39.36	172,831	39.94
Exercisable at end of year	42,171		18,114	

6. **Income Taxes**—Income tax expense is composed of the following (in thousands):

	1974	1973
Current:		
Federal	$37,733	$37,009
State and city	3,704	3,596
Foreign (principally Canadian)	1,851	1,505
	43,288	42,110
Deferred	(273)	(1,913)
	$43,015	$40,197
Investment tax credits	$ 912	$ 558

The tax effect of timing differences resulting in net deferred income taxes during the year ended February 28, 1974 arose from valuation reserves and accruals not currently deductible for tax purposes, $541,000, deferred compensation, $172,000 and adjustments resulting from reorganization of certain subsidiaries, $186,000, offset by accelerated methods of depreciation, $454,000, installment sales, $157,000, and other, net $15,000.

The Federal income tax returns of the company and its major subsidiaries for the three taxable years 1969 through 1971 are currently in the process of examination. Management is of the opinion that the results of these examinations will have no material effect on consolidated financial position or results of operations.

7. **Pension and Retirement Plans**—The company and its subsidiaries have pension plans covering substantially all employees. The company's policy with respect to principal pension plans is to fund pension costs accrued. Total pension expense was $7,875,000 in 1974 and $7,304,000 in 1973, which includes as to certain of the plans amortization of prior service costs over periods ranging from 20 to 40 years. The actuarially computed value of vested benefits as of latest valuation dates of the plans exceeds the total of the pension funds and balance sheet accruals by approximately $5,400,000.

8. **Lease Commitments**—Substantially all of the company's retail outlets and certain other real properties and equipment are operated under lease agreements expiring at various times through the year 2009. Leases covering retail outlets and equipment generally require, in addition to stated minimums, contingent rentals based on retail sales and equipment usage. Generally, the leases provide for renewal for various periods at stipulated rates.

Total rental expense was as follows (in thousands):

	1974	1973
Basic rentals	$25,275	$25,014
Contingent rentals	9,912	9,393
	35,187	34,407
Less sublease rentals	1,824	1,580
	$33,363	$32,827

Included in rental expense above is the cost of services provided by lessors of leased retail departments, estimated to aggregate $6,400,000 in 1974 and $5,900,000 in 1973.

At February 28, 1974, minimum rental commitments under all noncancelable leases, excluding capitalized leases, were as follows (in thousands):

	Type of Property		
Year	Real Property	Equipment	Total
1975	$ 19,648	$1,718	$ 21,366
1976	18,397	1,467	19,864
1977	16,893	1,081	17,974
1978	15,581	400	15,981
1979	13,885	96	13,981
1980-1984	51,891	4	51,895
1985-1989	27,026	—	27,026
1990-1994	10,487	—	10,487
1995-2009	4,195	—	4,195
	$178,003	$4,766	$182,769

The above minimum rental commitments for real property have been reduced by rentals from subleases. These subleases, expiring at various dates to 1993, provide for aggregate minimum rentals of approximately $7,700,000.

The present value of noncapitalized financing leases, as defined by the Securities and Exchange Commission, and the impact on net earnings if such leases had been capitalized are not material to the accompanying financial statements.

The company has also guaranteed leases of certain retail outlets of customers which at February 28, 1974 aggregates approximately $1,900,000 based on minimum rentals.

9. **Earnings Per Share of Common Stock**—Fully diluted earnings per share are based on the weighted average number of shares of common stock and common stock equivalents outstanding during the years, plus those common shares which would have been issued if conversion of all preferred stock had taken place at the beginning of each year. Common stock issuances based on profit performance and common stock options, the exercise of which would result in dilution of earnings per share, have been considered as the equivalent of common stock.

Primary earnings per share are based on those shares included in the fully diluted earnings per share calculations, except that conversion of preferred stock has not been assumed. Net earnings for this computation were reduced by preferred stock dividend requirements.

PEAT, MARWICK, MITCHELL & CO.
Certified Public Accountants
720 Olive Street
St. Louis, Missouri

THE BOARD OF DIRECTORS AND STOCKHOLDERS
INTERCO INCORPORATED:

We have examined the consolidated balance sheets of INTERCO INCORPORATED and subsidiaries as of February 28, 1974 and 1973 and the related consolidated statements of earnings, stockholders' equity, and changes in financial position for the years then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the aforementioned consolidated financial statements present fairly the financial position of INTERCO INCORPORATED and subsidiaries at February 28, 1974 and 1973 and the results of their operations, and the changes in their financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

April 12, 1974

Peat, Marwick, Mitchell & Co.

5 YEAR CONSOLIDATED FINANCIAL REVIEW

(Dollars in thousands except per share data)

	FISCAL YEARS ENDED				
	February 28			November 30	
FOR THE YEAR	1974	1973	1972	1970	1969
Net sales:					
Apparel	$ 281,148	$ 265,988	$ 228,768	$ 208,315	$ 165,716
General retail	363,176	342,630	312,141	255,236	225,652
Footwear	477,603	442,571	399,971	379,914	373,927
Total	1,121,927	1,051,189	940,880	843,465	765,295
Earnings before income taxes:					
Apparel	30,668	28,614	21,589	18,358	12,544
General retail	23,798	18,181	17,983	16,870	16,065
Footwear	45,697	43,642	37,219	34,589	33,229
	100,163	90,437	76,791	69,817	61,838
Less corporate expenses and interest cost	10,106	7,769	7,941	8,404	6,599
Total	90,057	82,668	68,850	61,413	55,239
As a percent of sales	8.0%	7.9%	7.3%	7.3%	7.2%
Net earnings	47,042	42,471	35,830	30,786	28,085
As a percent of sales	4.2%	4.0%	3.8%	3.6%	3.7%
Cash dividends paid:					
On common stock	13,619	12,229	10,837	8,239	7,300
On preferred stock	868	988	1,452	2,498	2,429
AT YEAR END					
Working capital	314,044	293,055	272,175	224,612	220,145
Property, plant and equipment, net	103,555	91,745	85,961	85,394	75,286
Capital expenditures	23,957	16,745	15,277	17,707	17,189
Total assets	546,900	510,884	480,810	444,759	398,907
Long-term debt	63,145	62,528	68,729	71,570	73,900
Stockholders' equity	359,350	327,228	294,540	244,247	222,843
PER SHARE OF COMMON STOCK					
Fully diluted earnings (1)	$ 4.11	$ 3.70	$ 3.17	$ 2.86	$ 2.66
Dividends	$ 1.32	$ 1.25	$ 1.21	$ 1.10	$ 1.00

(1) Refer to Earnings per Share of Common Stock in Notes to Consolidated Financial Statements.
(2) The above figures have been restated to include pooled companies for years prior to their acquisition.
(3) Fiscal 1974, 1973, and 1972 reflect the change in fiscal year from November 30 to the last day in February.

Directors

DAVID R. CALHOUN
Chairman of Executive Committee, First Union, Incorporated and Chairman of the Board, St. Louis Union Trust Company

MAURICE R. CHAMBERS
Chairman of the Board and Chief Executive Officer of the Company

STANLEY M. COHEN
President, Central Hardware Company

WEBSTER L. COWDEN
Chairman of the Board, Cowden Manufacturing Company

WILLIAM L. EDWARDS, JR.
Senior Executive Vice President and Chief Administrative Officer of the Company

RICHARD P. HAMILTON
President, The Florsheim Shoe Company

PHILIP N. HIRSCH
Chairman of the Board, P. N. Hirsch & Company

J. LEE JOHNSON
Retired

EDWIN S. JONES
Chairman of the Board and President, First Union, Incorporated and Chairman of the Board, First National Bank in St. Louis

SAMUEL S. KAUFMAN
Chairman of the Board, Campus Sweater & Sportswear Company

DONALD E. LASATER
Chairman of the Board, Mercantile Bancorporation Inc. and Mercantile Trust Company National Association

NORFLEET H. RAND
Vice Chairman of the Board and Treasurer of the Company

JOHN K. RIEDY
President and Chief Operating Officer of the Company

EDWARD J. RILEY
President, International Shoe Company

HERBERT SHAINBERG
Retired

Audit and Executive Compensation and Stock Option Committees

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DAVID R. CALHOUN
EDWIN S. JONES
DONALD E. LASATER

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JOHN K. RIEDY, President and Chief Operating Officer

NORFLEET H. RAND, Vice Chairman of the Board and Treasurer

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RONALD L. AYLWARD, Vice President and General Counsel

DUANE A. PATTERSON, Secretary

EDWARD P. GRACE, Assistant Treasurer

STANLEY F. HUCK, Assistant Controller

Corporate Offices

Ten Broadway
St. Louis, Missouri 63102

Transfer Agents

Manufacturers Hanover Trust Company
New York, New York

Mercantile Trust Company National Association
St. Louis, Missouri

Registrars

Morgan Guaranty Trust Company
New York, New York

St. Louis Union Trust Company
St. Louis, Missouri

Dividend Disbursing Agent

Mercantile Trust Company National Association
St. Louis, Missouri

INTERCO INCORPORATED

St. Louis, Missouri